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Debate on the Global Economy

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THURSDAY, October 13, 2022
2:00PM- 3:00PM, IMF HQ1 Atrium (HQ1-1-700)

Debate on the Global Economy

Sponsored by the IMF's Research Department

Inflation has hit levels not seen in decades, unleashing a cost of living crisis across the globe. At the same time, debt levels remain high, many vulnerable economies face increasing strains from tighter global financial conditions, and global fragmentation pressures are increasing. Policy makers face the tough choice of cooling the world economy to tame inflation at a time when growth is already weakening. Join the CNN Global debate to hear more at this critical hour for the world economy.

Agarwal, Ruchir, and Miles Kimball. 2022.

"Will Inflation Remain High?" *Finance & Development*, April.

The recent increase in inflation worldwide took many by surprise. As of early 2022, both headline inflation (price of all goods and services) and core inflation (excluding food and energy) were significantly above target in most advanced economies and several emerging markets. Standard economic theory states that inflation will get out of control under a prolonged mix of certain monetary and fiscal policies, but whether inflation will persist toward that end warrants further examination. The answer depends both on the distribution of shocks to the economy and how central banks (and finance ministries) react.

Albagli Elías, Francesco Grigoli, and Emiliano Luttini. 2022.

"Inflation Expectations and the Supply Chain." Working Paper No. 2022/161, International Monetary Fund, Washington, DC.

We show that firms rely on price changes observed along their supply chain to form expectations about aggregate inflation, and that these expectations have a complete pass-through to sales prices. Leveraging a unique dataset on Chilean firms merging expectation surveys and records from the VAT and customs registries, we document that changes in prices at which firms purchase inputs inform their forecasts of the economy's inflation. This is the case even if changes in input costs do not determine the inflation outcome. These findings reject the full-information rational-expectations hypothesis and are consistent with firms' disagreement about future inflation and inattention to macroeconomic news, which we document for Chile. Our results from a firm-level Phillips' curve estimation suggest that firms' beliefs about inflation are a key determinant for their price-setting decisions. Therefore, we argue that the channel we highlight in this paper has the potential to lead to dispersion in inflation expectations, price dispersion, and weaken the expectation channel of policies.

Amaglobeli, David, Emine Hanedar, Gee Hee Hong, and Celine Thevenot. 2022.

"Fiscal Policy for Mitigating the Social Impact of High Energy and Food Prices." IMF Notes No 2022/001, International Monetary Fund, Washington, DC.

Fiscal policy has a crucial role in lessening the impact on the most vulnerable households. Governments must balance by ensuring access to energy and food, normalizing fiscal policy after unprecedented support in 2020, and promoting green transformation.

Banerjee, Ryan Niladri, Valerie Boctor, Aaron Mehrotra, and Fabrizio Zampolli. 2022.

"Fiscal Deficits and Inflation Risks: the Role of Fiscal and Monetary Policy Regimes." BIS Working Papers No 1028, Bank for International Settlements, Basel.

Using data from a panel of advanced economies over four decades, we show that the inflationary effect of fiscal deficits crucially depends on the prevailing fiscal-monetary policy regime. Under fiscal dominance, defined as a regime in which the government does not adjust the primary balance to stabilise debt and the central bank is less independent or puts less emphasis on price stability, the average effect on inflation of higher deficits is found to be up to five times larger than under monetary dominance. Under fiscal dominance, higher deficits also increase the dispersion of possible future inflationary outcomes, especially the probability of high inflation. Based on forecasts from our model, the high inflation experienced by many countries during the recovery from the Covid-19 pandemic appears more consistent with a regime of fiscal dominance than monetary dominance.

Carriere-Swallow, Yan, Pragyan Deb, Davide Furceri, Daniel Jimenez, and Jonathan David Ostry. 2022.

"Shipping Costs and Inflation." Working Paper No. 2022/061, International Monetary Fund, Washington, DC.

The Covid-19 pandemic has disrupted global supply chains, leading to shipment delays and soaring shipping costs. We study the impact of shocks to global shipping costs—measured by the Baltic Dry Index (BDI)—on domestic prices for a large panel of countries during the period 1992-2021. We find that spikes in the BDI are followed by sizable and statistically significant increases in import prices, PPI, headline, and core inflation, as well as inflation expectations. The impact is similar in magnitude but more persistent than for shocks to global oil and food prices. The effects are more muted in countries where imports make up a smaller share of domestic consumption, and those with inflation targeting regimes and better anchored inflation expectations. The results are robust to several checks, including an instrumental variables approach in

which we instrument changes in shipping costs with an indicator of closures of the Suez Canal.

Engler, Philipp, Roberto Piazza, and Galen Sher. 2021.

"How Rising Interest Rates Could Affect Emerging Markets." *IMFBlog*, April 5.

Rapid vaccine rollout in the United States and passage of its $1.9 trillion fiscal stimulus package have boosted its expected economic recovery. In anticipation, longer-term US interest rates have risen rapidly, with the rate on 10-year Treasury securities going from under 1 percent at the start of the year to over 1.75 percent in mid-March. A similar surge has occurred in the United Kingdom. In January and February, interest rates also rose somewhat in the euro area and Japan before central banks there stepped in with easier monetary policy.

Guénette, Justin Damien, M. Ayhan Kose, and Naotaka Sugawara. 2022.

"Is a Global Recession Imminent?" EFI Policy Note No.4., World Bank, Washington, DC.

Global growth prospects have deteriorated significantly since the beginning of the year, raising the specter of global recession. This paper relies on insights gleaned from previous global recessions to analyze the recent evolution of economic activity and policies and presents plausible scenarios for the global economy in 2022–24. We report three major findings. First, every global recession since 1970 was preceded by a significant weakening of global growth in the previous year, as has happened recently. Second, the global economy is in the midst of one of the most internationally synchronous episodes of monetary and fiscal policy tightening of the past five decades. The policy actions in many countries are necessary to contain inflationary pressures, but their mutually compounding effects could have larger impacts than envisioned—both in tightening financial conditions and in steepening the global growth slowdown. Third, if the degree of global monetary policy tightening markets now expect is not enough to reduce inflation to targets, experience from previous global recessions suggests that the additional tightening needed could cause significant financial stress and increase the likelihood of a global recession next year. These findings imply that policymakers need to carefully calibrate, clearly communicate, and credibly implement their policy actions while considering potential international spillovers, especially given the globally synchronous withdrawal of monetary and fiscal policies.

Guerreiro, Vanda, Andrew Baer, and Anthony Silungwe. 2022.

"The Availability, Methodological Soundness, and Scope of Consumer Price Statistics in 2020." Working Paper No. 2022/053, International Monetary Fund, Washington, DC.

This paper analyzes the availability, methodological soundness, and scope of Consumer Price statistics in IMF member and non-member countries in 2020. Consumer price statistics are instrumental in the development of monetary policy and in monitoring economic developments. They also often have administrative uses such as in determine wage increase or seting pension payments. This analysis examines the appropriateness of the current set of global consumer price statistics for current policy development and highlights regions where further development may be required. The analysis is based on the results of a new annual survey of CPI compilation practices in 207 economies as of the end of 2020. The survey was completed by statistical authorities between March 2021 and June 2021. In cases of non-response, IMF staff estimates were used. IMF Staff estimates were based on information taken from the IMF's Dissemination Standards Bulletin Board (DSBB) and country websites to provide the status of consumer price index compilation practices. These data summarize the following key aspects; i) Production, publication and scope of the Consumer Price Index Program, ii) Data sources, iii) CPI compilation methods and iv) Concepts and classifications.

Graf, Brian. 2020.

"Consumer Price Index Manual: Concepts and Methods." Manuals & Guides, International Monetary Fund, Washington, DC.

The Consumer Price Index Manual: Concepts and Methods contains comprehensive information and explanations on compiling a consumer price index (CPI). The Manual provides an overview of the methods and practices national statistical offices (NSOs) should consider when making decisions on how to deal with the various problems in the compilation of a CPI. The chapters cover many topics. They elaborate on the different practices currently in use, propose alternatives whenever possible, and discuss the advantages and disadvantages of each alternative. The primary purpose

of the Manual is to assist countries in producing CPIs that reflect internationally recommended methods and practices.

Kohlscheen, Emanuel. 2021.

"[What Does Machine Learning Say About the Drivers of Inflation?]" BIS Working Papers No 980, Bank for International Settlements, Basel.

This paper examines the drivers of CPI inflation through the lens of a simple, but computationally intensive machine learning technique. More specifically, it predicts inflation across 20 advanced countries between 2000 and 2021, relying on 1,000 regression trees that are constructed based on six key macroeconomic variables. This agnostic, purely data driven method delivers (relatively) good outcome prediction performance. Out of sample root mean square errors (RMSE) systematically beat even the in-sample benchmark econometric models, with a 28% RMSE reduction relative to a naïve AR(1) model and a 8% RMSE reduction relative to OLS. Overall, the results highlight the role of expectations for inflation outcomes in advanced economies, even though their importance appears to have declined somewhat during the last 10 years.

Liu, Yang, Di Yang, and Yunhui Zhao. 2022.

"[Housing Boom and Headline Inflation: Insights from Machine Learning]." *Working Paper* No. 2022/151, International Monetary Fund, Washington, DC.

Inflation has been rising during the pandemic against supply chain disruptions and a multi-year boom in global owner-occupied house prices. We present some stylized facts pointing to house prices as a leading indicator of headline inflation in the U.S. and eight other major economies with fast-rising house prices. We then apply machine learning methods to forecast inflation in two housing components (rent and owner-occupied housing cost) of the headline inflation and draw tentative inferences about inflationary impact. Our results suggest that for most of these countries, the housing components could have a relatively large and sustained contribution to headline inflation, as inflation is just starting to reflect the higher house prices. Methodologically, for the vast majority of countries we analyze, machine-learning models outperform the VAR model, suggesting some potential value for incorporating such models into inflation forecasting.

Okou, Cedric, John Spray, and D. Filiz Unsal. 2022.

"[Africa Food Prices Are Soaring Amid High Import Reliance]." *IMFBlog*, September 27.

Factors include the region's heavy reliance on food imports and changes in food consumption and incomes. Staple food prices in sub-Saharan Africa surged by an average 23.9 percent in 2020-22—the most since the 2008 global financial crisis. This is commensurate to an 8.5 percent rise in the cost of a typical food consumption basket (beyond generalized price increases). Global factors are partly to blame. Because the region imports most of its top staple foods—wheat, palm oil, and rice—the pass-through from global to local food prices is significant, nearly one-to-one in some countries.

Peterson Institute for International Economics. 2019.

"[The Future of the Global Economy: Integration or Fragmentation?]" American Economic Association panel discussion held at the 2019 Allied Social Science Association annual meeting, January 5, 2019.

Adam S. Posen participated in the American Economic Association (AEA) panel discussion "The Future of the Global Economy: Integration or Fragmentation?" held at the 2019 Allied Social Science Association (ASSA) annual meeting. David Lipton, first deputy managing director of the International Monetary Fund, chaired the session.

Other panelists included Yiping Huang, China Center for Economic Research, Peking University; Kristin J. Forbes, Jerome and Dorothy Lemelson Professor of Management and Global Economics, MIT; and Jay Shambaugh, professor of economics and international affairs, Elliott School of International Affairs, George Washington University, and Brookings Institution.

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